This notice was revoked on April 13, 2009 by Revenue Notice # 09-04.

MINNESOTA DEPARTMENT OF REVENUE

Revenue Notice # 05-07: Sales and Use Tax – Bad Debts; Deductions of Uncollectible Debts; Applying Payments Received on Previously Claimed Bad Debt

This revenue notice sets forth the Department's position on "bad debt" deductions from sales and use tax for debt that is written off as uncollectible in the claimant's books and records and that is either eligible to be deducted for federal income tax purposes or, under generally accepted accounting principles, would be eligible for a bad debt deduction for federal income tax purposes if the claimant was required to file a federal income tax return.

This revenue notice also sets forth the Department's position on the treatment of a debt payment made subsequent to the taxpayer deducting a "bad debt," regarding the apportionment of the payment among the taxable price of the product, the sales tax, and any other charges imposed on the customer.

Statutory and Regulatory Authority

Under Minnesota Statutes, section 297A.81, "bad debts," as defined and limited by section 289A.40, subdivision 2, may be deducted on the taxpayer's sales tax return for the period during which the bad debt is written off as uncollectible. Minnesota Rules, part 8130.7400, subpart 1, provides the general rule that uncollectible debts ("bad debts") will be recognized as a deduction for sales tax purposes only when given recognition by a direct charge-off for federal income tax purposes or, if the retailer is not required to file income tax returns, the bad debt will be charged off "in accordance with generally accepted accounting principles."

Minnesota Rules, part 8130.7400, subpart 5, provides that if a taxpayer collects a debt in whole or in part after the taxpayer had previously deducted the bad debt on a sales tax return, then the amount collected must be included in the first return filed after collection, and the tax on the amount must be paid with the return.

Department Position

A. Deductions of Uncollectible Debts

If a taxpayer is required to file federal income tax returns, bad debts may be deducted on the sales and use tax return for the period during which the following two criteria are met:

1. the bad debt is written off as uncollectible in the claimant's books and records, and
2. the bad debt is eligible to be deducted for federal income tax purposes.

The Department interprets meeting these criteria as meeting the test of Minnesota Rules, part 8130.7400, subpart 1, that only a debt that has been "given recognition by a direct charge-off" on the claimant's books and records "for federal income tax purposes" may be deducted.

If a taxpayer is not required to file federal income tax returns, bad debts may be deducted on the sales and use tax return for the period during which the above two criteria are met, as if the claimant was required to file a federal income tax return, or as long as the debt is otherwise charged off "in accordance with generally accepted accounting principles."

B. Applying Payments Received on Previously Claimed Bad Debt

For the purposes of reporting a payment received on a previously claimed bad debt, any payments made on a debt or account are applied first proportionally to the taxable price of the property or service and the sales tax thereon, and secondly to interest, service charges, and any other charges.

JOHN H. MANSUN, Assistant Commissioner
for Tax Policy and External Relations

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